

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

RICHARD WOOL and ALLAN
MAYER, on behalf of the Sitrick and
Company Employee Stock Ownership
Plan,

Plaintiffs,

vs.

MICHAEL S. SITRICK and NANCY
SITRICK, husband and wife; THE
MICHAEL AND NANCY SITRICK
TRUST, a trust; RELIANCE TRUST
COMPANY, a Georgia corporation;

Defendants,

SITRICK AND COMPANY, INC., a
California corporation; SITRICK
AND COMPANY EMPLOYEE
STOCK OWNERSHIP PLAN;

Nominal Defendants.

Case No. 2:10-cv-02741-JHN-PJWx

**ORDER GRANTING IN PART AND
DENYING IN PART THE
SITRICKS' MOTION TO DISMISS
AND RELIANCE'S MOTION TO
DISMISS**

Judge: Honorable Jacqueline H. Nguyen

The matters before the Court are the Sitrick Defendants' Motion to Dismiss the First Amended Complaint ("Sitricks' Motion") (Docket No. 29) and the Reliance Trust Company's Motion to Dismiss First Amended Complaint ("Reliance's Motion") (Docket No. 30), both of which were filed on June 21, 2010. The Court took both matters under submission on August 5, 2010.

(Docket No. 48.) The Court has considered the briefs filed in these matters, and for the reasons herein, the Court GRANTS IN PART and DENIES IN PART the Sitricks' Motion. The Court GRANTS the Sitricks' Motion and dismisses *without prejudice* Count I, Count II (with respect to the Personal Goodwill Transaction only) and Count III as alleged against Sitrick and Nancy Sitrick. The Court DENIES the Sitricks' Motion as to all remaining claims.

Additionally, the Court GRANTS IN PART and DENIES IN PART Reliance's Motion. The Court GRANTS Reliance's Motion and dismisses *without prejudice* Count III as alleged against Defendant Reliance. The Court DENIES Reliance's Motion as to all remaining claims.

I.

FACTUAL BACKGROUND

In 1989, Defendant Michael S. Sitrick ("Sitrick") founded Sitrick and Company, Inc. ("SCI"), a company providing "strategic communication services" to various businesses, agencies, and individuals. (First Am. Compl. ("FAC") ¶¶ 3, 7, 12.) Sitrick was SCI's sole shareholder. (*Id.* at ¶ 18.)

A. The Employee Stock Ownership Plan

On March 1, 1999, SCI established the Sitrick and Company Employee Stock Ownership Plan ("ESOP") and the Employee Stock Ownership Trust ("ESOT"). (FAC ¶ 17.) "The ESOP is a stock bonus plan qualified under § 401(a) of the Internal Revenue Code of 1986 as amended and is an employment stock ownership plan as defined under ERISA." (*Id.*) SCI appointed Sitrick as the ESOP's sole trustee and issued 1,702,400 shares of Class B stock to Sitrick. (*Id.* at ¶ 19–21.) Sitrick sold all those shares of Class B stock to the ESOP for approximately \$15,321,600 or \$9.00 per share. (*Id.* at ¶ 22.) This transaction left the ESOP with 24.32% of the total equity in SCI, while Sitrick owned the remaining equity in SCI through his Class A shares. (*Id.*) SCI financed the stock purchase by borrowing the amount of the purchase price and loaning it to the

1 ESOP. (*Id.* at ¶ 23.) “The ESOP paid Sitrick for the Class B shares and executed
 2 and delivered to SCI a promissory note payable in installments of principal and
 3 interest.” (*Id.*) Plaintiffs allege that “the total equity of the SCI exceeded the sum
 4 of \$60 million in or about March 1999.” (*Id.* at ¶ 25.)

5 From 2001 to 2008, SCI “continued to grow and prosper” with, for
 6 instance, over \$22.5 million in total revenues for the year ending December 31,
 7 2008. (FAC ¶ 29.) However, “[d]espite the profitability and growth of the
 8 Company, as well as the reduction of the ESOP indebtedness each year, the ESOP
 9 reported to its participants and beneficiaries a decline in the value of Plan assets
 10 and share value virtually every year from 2001 to 2008.” (*Id.* at ¶ 30.) “As a
 11 result, the gross value of Plan assets declined from a reported high of
 12 approximately \$17.36 million in 2000, to a reported low of approximately \$1.7
 13 million in 2008, despite the fact that the original ESOP indebtedness of
 14 approximately \$15.3 million was almost fully repaid by December 31, 2008.”
 15 (*Id.* at ¶ 31.)

16 Plaintiffs contend that this loss of nearly 90% of the ESOP’s original fair
 17 market value resulted, in large part, from “self-dealing by Sitrick and [a] breach
 18 of his fiduciary duties as trustee of the ESOP.” (FAC ¶ 32.) In particular,
 19 Plaintiff contends the loss stemmed from a “Personal Goodwill Transaction” and
 20 the “2008 Stock Repurchase Transaction.” (*Id.* ¶¶ 33–64.)

21 **B. The Personal Goodwill Transaction**

22 The Personal Goodwill Transaction (or “Transaction”) “was a conflicted
 23 transaction in which Sitrick acted in both his individual capacity and his corporate
 24 capacity as SCI Chief Executive Officer and Director in approving the
 25 Transaction and in agreeing to annual royalty payments.” (FAC ¶ 37.) The
 26 Transaction consisted of a “verbal or written royalty agreement” between Sitrick
 27 and SCI, wherein “SCI was granted the nonexclusive and revocable right to use
 28 Sitrick’s Personal Goodwill in consideration for an annual royalty payment to

1 Sitrick.” (*Id.* at ¶ 36.) Sitrick purportedly received millions of dollars pursuant to
2 the terms of the Transaction and concealed those royalty payments from ESOP
3 participants. (*Id.* at ¶¶ 38–39.) Plaintiff claims the Transaction was “an improper
4 misappropriation and diversion of corporation assets” (*id.* at ¶ 40), that “Sitrick in
5 his capacity as ESOP Trustee never objected to the Personal Goodwill
6 Transaction” (*id.* at ¶ 42), and that the Transaction “substantially diluted the value
7 of SCI’s assets and employer securities owned by the ESOP” (*id.* at ¶ 43).

8 **C. The 2008 Stock Repurchase Transaction**

9 With respect to the 2008 Stock Repurchase Transaction (or “Stock
10 Repurchase”), Sitrick allegedly learned of an offer from Resources Connection,
11 Inc. (“Resources”) to purchase SCI assets or stock for an amount in excess of \$70
12 million. (FAC ¶ 44.) Upon learning of this lucrative offer, Sitrick purportedly
13 “conceived the plan to purchase all of the ESOP’s stock in SCI for a fraction of
14 its fair market value and thereafter to sell the SCI assets and his Personal
15 Goodwill to Resources for a sum approaching \$90 million or more.” (*Id.* at ¶ 45.)

16 “To carry out his plan, Sitrick caused the SCI Board of Directors to engage
17 [Defendant Reliance Trust Company (“Reliance”)] as an independent fiduciary
18 for the ESOP to consider and approve the sale of all of the ESOP’s Class B shares
19 in SCI to the [Defendant The Michael and Nancy Sitrick Trust (“Sitrick Trust”)]
20 and to engage an unknown financial advisor to prepare a valuation and/or fairness
21 opinion to support the Transaction.” (FAC ¶ 46.) According to the FAC, Sitrick
22 “intentionally failed to disclose information or made false or misleading
23 statements of facts which were material to the fairness of the proposed [Stock
24 Repurchase] and the fair market value of ESOP’s Class B shares.” (*Id.* at ¶ 48.)
25 “By reason of such omissions and/or false or misleading statements,” Plaintiffs
26 claim, “Defendants Sitrick and [his wife] Nancy Sitrick were de facto
27 discretionary fiduciaries for the Stock Repurchase Transaction, by omission or
28 misrepresentation.” (*Id.* (emphasis omitted).) Although the FAC does not allege

any specific false or misleading statements by Nancy Sitrick, the FAC does state that Sitrick “failed to disclose or misrepresented the substantial offers to purchase SCI by multiple companies sine 2000, the formal or informal offers to acquire SCI made by Resources in 2007 and 2008, and the conflicts and prohibited transaction in which Sitrick engaged with respect to the Personal Goodwill Transaction.” (*Id.* at ¶ 49.)

In terms of Reliance’s purported liability, the FAC claims that Reliance failed to conduct a “careful and prudent investigation” into the circumstances surrounding the Stock Repurchase and “failed to determine in good faith the fair market value of the ESOP’s Class B shares.” (FAC ¶ 50.) “Instead, Reliance and its financial advisor assumed that the Personal Goodwill Transaction was contractual, valid, and binding and determined that the ESOP’s Class B shares had a total aggregate value of only \$1.04 per share or approximately \$1.7 million.” (*Id.* at ¶ 51.)

As a result of the Stock Repurchase, Plaintiffs allege that the valuation of the ESOP’s Class B shares was “a colossal understatement” of their fair market value and that the ESOP received “far less than adequate consideration in this prohibited transaction between the ESOP and parties in interest.” (FAC ¶¶ 55–56.)

II.

PROCEDURAL HISTORY

On April 15, 2010, Plaintiffs Richard Wool and Allan Mayer (collectively “Plaintiffs”) filed this lawsuit on behalf of the ESOP. Plaintiffs filed their FAC on May 15, 2010 against Defendants Sitrick, Nancy Sitrick, the Sitrick Trust, and Reliance and Nominal Defendants SCI and the ESOP. Plaintiffs assert the following causes of action under The Employee Retirement Income Security Act of 1974 (“ERISA”), 29 U.S.C. § 1001 *et seq.*:

- (1) violation of Section 404 of the ERISA, 29 U.S.C. § 1104, against

- 1 Sitrick, Nancy Sitrick, and Reliance;
- 2 (2) violation of Sections 406 and 408 of the ERISA, 29 U.S.C. §§ 1106
- 3 and 1108, against Sitrick, Nancy Sitrick, the Sitrick Trust, and
- 4 Reliance;¹
- 5 (3) violation of Section 405 of the ERISA, 29 U.S.C. § 1105, against
- 6 Sitrick, Nancy Sitrick, and Reliance; and
- 7 (4) equitable remedies under Sections 409(a) and 501(a)(3) of the
- 8 ERISA, 29 U.S.C. §§ 1109(a) and 1132(a)(3), against the Sitrick
- 9 Trust.
- 10 (FAC ¶¶ 65–95.)

11 On June 21, 2010, Defendants filed two motions to dismiss. The first is the

12 Sitricks' Motion for dismissal of all claims against the Sitrick

13 Defendants—Sitrick, Nancy Sitrick, and the Sitrick Trust. In support of their

14 Motion, the Sitrick Defendants filed a supporting Memorandum ("Sitricks'

15 Mem.") and a Request for Judicial Notice ("Sitricks' RFJN").

16 The second pending motion to dismiss is Reliance's Motion, which seeks

17 dismissal of all claims against Reliance. In addition to its Motion, Reliance filed

18 a supporting Memorandum ("Reliance's Mem.") and a Request for Judicial

19 Notice ("Reliance's RFJN").

20 Plaintiffs subsequently filed a separate Opposition to each Motion ("Opp'n

21 to Sitricks' Mot." and "Opp'n to Reliance's Mot." respectively), along with a

22 Request for Judicial Notice ("Pls.' RFJN"). Defendants thereafter filed a Reply

23 ("Sitricks' Reply" and "Reliance's Reply" respectively).

24 ///

25 III.

26

27 ¹ Although the header does not indicate that Count II is against Reliance,

28 Paragraphs 78 and 80 indicate that Count II is alleged against Reliance as well.

REQUESTS FOR JUDICIAL NOTICE

All parties have requested the Court take judicial notice of various documents. Judicial notice is appropriate under Federal Rule of Evidence 201 for facts “not subject to reasonable dispute,” because they are either “generally known within the territorial jurisdiction of the trial court” or “capable of accurate and ready determination by resort to sources whose accuracy cannot reasonably be questioned.” Fed. R. Evid. 201(b). Judicial notice is also appropriate for documents on which the complaint necessarily relies and also for matters of public record, provided that the authenticity of the documents is not reasonably contested. *Lee v. City of Los Angeles*, 250 F.3d 668, 688–89 (9th Cir. 2001).

A. Sitricks’ Request for Judicial Notice

The Sitrick Defendants request that the Court take judicial notice of two Exhibits. Exhibit A is the “Resources Connection, Inc. Form 8-K Report filed with the Securities and Exchange Commission (‘SEC’) and signed and dated October 29, 2009 (‘Resources Form 8-K’), accessible from the SEC’s online ‘EDGAR’ database available at www.sec.gov.” (Sitricks’ RFJN 1.) Exhibit B is the “The December 23, [2]008 Redemption Agreement referred to in the [FAC] as the ‘Stock Repurchase Transaction.’” (*Id.*)

Exhibit A is a copy of a document filed with the SEC and appears to be capable of accurate and ready determination. *In re Copper Mt. Secs. Litig.*, 311 F. Supp. 2d 857, 863 (N.D. Cal. 2004) (finding that documents filed with the SEC are appropriate for judicial notice). Exhibit B is a document necessarily relied upon in the FAC. Because both Exhibits are documents appropriate for judicial notice, Plaintiffs do not oppose the Court taking judicial notice, and Plaintiffs do not dispute the Exhibits’ authenticity, the Court GRANTS the Sitrick Defendants’ Request and takes judicial notice of Exhibits A and B.

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B. Reliance’s Request for Judicial Notice

1 Reliance requests that the Court take judicial notice of Exhibit A, the BCC
 2 Valuation Report purportedly relied upon by Reliance during the valuation
 3 process of SCI and the Class B stock. (Reliance's RFJN 1–2.) Reliance claims
 4 Exhibit A is necessarily relied upon in the FAC, an argument which Plaintiffs
 5 dispute. (*Id.*) Regardless of whether the FAC necessarily relies on Exhibit A,
 6 Plaintiffs dispute its authenticity. (Opp'n to Reliance's Mot. 7–8.) Plaintiffs
 7 claim the Report is a “private document never before revealed to the ESOP
 8 participants” and that they have no means of verifying its accuracy at this stage.
 9 (*Id.* at 8.) Because the document's authenticity is reasonably in dispute, the
 10 Court DENIES Reliance's Request and declines to take judicial notice of Exhibit
 11 A.

12 **C. Plaintiffs' Request for Judicial Notice**

13 Finally, in support of its Opposition to Reliance's Motion, Plaintiffs
 14 request that this Court take judicial notice of Exhibit A, the SCI Financial
 15 Statement as of December 31, 2008 (audited) and June 30, 2009 (unaudited),
 16 which was filed with the SEC. (Pls.' RFJN 2.) Exhibit A is a copy of a
 17 document filed with the SEC, and its authenticity has not been questioned. As
 18 such, the Court GRANTS Plaintiffs' Request and takes judicial notice of Exhibit
 19 A. *In re Copper Mt. Secs. Litig.*, 311 F. Supp. 2d at 863.

20 **IV.**

21 **LEGAL STANDARD**

22 Rule 12(b)(6) permits a defendant to seek dismissal of a complaint that
 23 “fail[s] to state a claim upon which relief can be granted.” Fed. R. Civ. P.
 24 12(b)(6). In evaluating a motion to dismiss, the Court generally cannot consider
 25 material outside the complaint, such as facts presented in briefs, affidavits, or
 26 discovery materials, unless such material is alleged in the complaint or judicially
 27 noticed. *McCalip v. De Legarret*, No. CV 08-2250 CAS (FFMx), 2008 U.S. Dist.
 28 LEXIS 87870, at *4 (C.D. Cal. Aug. 18, 2008); *see Jacobson v. AEG Capital*

1 *Corp.*, 50 F.3d 1493, 1496 (9th Cir. 1995). The Court must accept as true all
2 material factual allegations in the complaint and construe them in the light most
3 favorable to the plaintiff. *Nursing Home Pension Fund, Local 144 v. Oracle*
4 *Corp.*, 380 F.3d 1226, 1229 (9th Cir. 2004). However, this tenet is inapplicable
5 to legal conclusions. *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1949 (2009). The Court
6 need not accept as true “[t]hreadbare recitals of the elements of a cause of action,
7 supported by mere conclusory statements...” *Id.* The Court, based on judicial
8 experience and common-sense, must determine whether a complaint plausibly
9 states a claim for relief. *Id.* at 1950.

10 Part of the Court’s determination as to whether a claim plausibly states a
11 claim for relief involves an analysis of a pleading’s factual specificity. Asserting
12 more than mere conclusory statements, a complaint must provide a factual basis
13 showing that a plaintiff is entitled to relief and to give the defendant fair notice of
14 claims and relief asserted. *Id.* at 1950–51; *Bell Atl. Corp. v. Twombly*, 550 U.S.
15 544, 556 (2007); Fed. R. Civ. P. 8(a)(2). Although a lengthy factual background
16 is unnecessary, dismissal of a complaint is warranted where the plaintiff fails to
17 allege specific facts needed to support the plausibility of a claim or provide fair
18 notice to the opposing party. *See id.*

19 Dismissal is also warranted where a complaint, alleging fraud, fails to meet
20 the heightened pleading standards of Federal Rule of Civil Procedure 9(b).
21 Although “[m]alice, intent, knowledge, and other conditions of a person’s mind
22 may be alleged generally,” a complaint “must state with particularity the
23 circumstances constituting fraud or mistake.” Fed. R. Civ. P. 9(b). “Averments
24 of fraud must be accompanied by ‘the who, what, when, where, and how’ of the
25 misconduct charged.” *Vess v. Ciba-Geigy Corp. USA*, 317 F.3d 1097, 1106 (9th
26 Cir. 2003) (citation omitted). This includes allegations as to the particular
27 statement and why it was false or misleading. *Id.* In fact, “[t]he requirement of
28 specificity in a fraud action against a corporation requires the plaintiff to allege

the names of the persons who made the allegedly fraudulent representations, their authority to speak, to whom they spoke, what they said or wrote, and when it was said or written.” *Tarmann v. State Farm Mut. Auto. Ins. Co.*, 2 Cal. App. 4th 153, 157 (Cal. Ct. App. 1991). Failure to sufficiently allege fraud claims mandates their dismissal. *Vess*, 317 F.3d at 1106.

V.

DISCUSSION

A. Sitricks’ Motion to Dismiss

The Sitrick Defendants seeks dismissal of all claims under Federal Rules of Civil Procedure 8, 9(b), and 12(b)(6). (Sitricks’ Mot. I.) For the reasons herein, the Court dismisses *without prejudice* Counts I, II as it relates to the Personal Goodwill Transaction, and III, as alleged against Sitrick and Nancy Sitrick. The Court declines to dismiss the remaining claims.

1. Count I

Plaintiffs assert Count I—for violation of Section 404 of the ERISA, 29 U.S.C. § 1104—against Sitrick, Nancy Sitrick, and Reliance.² Section 404 imposes many duties upon ERISA fiduciaries, including the obligation to discharge one’s duties “with respect to a plan solely in the interest of the participants and beneficiaries” and “with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims.” 29 U.S.C. § 1104(a).

a. ERISA Fiduciaries

The Sitrick Defendants argue that Plaintiffs fail to state a claim under Section 404 on the ground that Sitrick and Nancy Sitrick were not ERISA fiduciaries. (Sitricks’ Mem. 7.) For instance, because the FAC alleges that

² The Sitricks’ Trust is not a named defendant for purposes of Count I.

1 Reliance was an “independent fiduciary” hired to consider and approve the Stock
2 Repurchase (FAC ¶ 46), the Sitrick Defendants contend there is no factual basis
3 to support the allegation that Sitrick and his wife were ERISA fiduciaries with
4 respect to the Stock Repurchase. The Court disagrees.

5 With regard to Sitrick, the FAC explicitly alleges that he was the ESOP’s
6 sole trustee (FAC ¶ 19) and does not contend that Sitrick was ever relieved of
7 that duty. Because ESOP trustees are fiduciaries, Sitrick was a fiduciary here.
8 *Johnson v. Couturier*, 572 F.3d 1067, 1076 (9th Cir. 2009) (“Because all three
9 Defendants served as ESOP trustees, each was an ERISA fiduciary subject to the
10 duties of loyalty and care and to the prohibition against self-dealing.”). Although
11 the SCI Board of Directors, of which Sitrick was a member (FAC ¶ 3), hired
12 Reliance to consider and approve the Stock Repurchase for the ESOP (*id.* at ¶
13 46), such does not alleviate Sitrick of his fiduciary duties owed to the ESOP.
14 *Howard v. Shay*, 100 F.3d 1484, 1489–90 (9th Cir. 1996) (“An independent
15 appraisal ‘is not a magic wand that fiduciaries may simply wave over a
16 transaction to ensure that their responsibilities are fulfilled...’”) (citation omitted).
17 Nothing in the FAC supports Defendants’ contention that Reliance became the
18 sole fiduciary of the ESOP. (Sitricks’ Reply 2.)

19 With respect to Nancy Sitrick, the FAC alleges that she was an officer and
20 director of SCI. (FAC ¶ 3.) Although not a formal trustee of the ESOP, the FAC
21 alleges that she, along with Sitrick, “acted with discretionary authority in
22 structuring, approving, and executing” various transactions, including the Stock
23 Repurchase. (*Id.* at ¶ 67.) Because ERISA defines a fiduciary liberally to include
24 any individual who exercises control, discretion, and authority over the
25 management or disposition of ESOP assets (*Johnson*, 572 F.3d at 1076), the FAC
26 provides an adequate factual basis to conclude that Nancy Sitrick was an ESOP
27 fiduciary for purposes of the Stock Repurchase. For the same reasons the
28 appointment of Reliance did not relieve Sitrick of his fiduciary duties, it similarly

1 did not relieve Nancy Sitrick of hers.

2 *b. Rule 9(b)*

3 Having found that the FAC adequately alleges that Sitrick and his wife
4 were fiduciaries, the Court now must address the Sitrick Defendants' second
5 argument—that the alleged misrepresentations and omissions do not support a
6 breach of fiduciary duty claim. (Sitricks' Mem. 9.) They contend that Plaintiffs'
7 claims are not pled with particularity as required by Federal Rule of Civil
8 Procedure 9(b). The Court agrees.

9 With respect to claims against Sitrick, the Court agrees that Plaintiffs have
10 failed to meet the heightened pleading requirements of Rule 9(b) for fraud claims.
11 "Fraud arises from the plaintiff's reliance on the defendant's false representations
12 of material fact, made with knowledge of falsity and the intent to deceive."
13 *Concha v. London*, 62 F.3d 1493, 1503 (9th Cir. 1995).

14 While Plaintiffs do allege breaches of fiduciary duty not necessarily tied to
15 fraudulent conduct (FAC ¶ 69), Plaintiffs' claims against Sitrick are grounded in
16 fraud. For instance, with regard to the Stock Repurchase, Plaintiffs allege that
17 Sitrick "conceived [a] plan" to repurchase the ESOP stock for his personal
18 financial gain and "carr[ied] out his plan" by "caus[ing]" SCI to hire Reliance.
19 (*Id.* at ¶¶ 44–46.) Plaintiffs allege that Sitrick "*intentionally* failed to disclose
20 information or made false or misleading statements of fact which were material to
21 the fairness of the [Stock Repurchase]." (*Id.* at ¶ 48 (emphasis added).) Yet,
22 while Plaintiffs' claims are rooted in fraud, Plaintiffs' general allegations in
23 Paragraph 69 of the FAC, regarding Sitrick's purported breaches of fiduciary
24 duty, fail to identify the particular circumstances constituting Sitrick's fraud.
25 Fed. R. Civ. P. 9(b). The FAC is lacking specific allegations as to "the who,
26 what, when, where, and how' of the misconduct charged." *Vess*, 317 F.3d at
27 1106 (citation omitted). Accordingly, the Court finds that Count I, as against
28 Sitrick, fails to meet the heightened pleading standards required under Rule 9(b).

1 With regard to Plaintiffs' claims against Nancy Sitrick, it is less clear
 2 whether Plaintiffs are alleging fraud. Although the FAC does not blatantly assert
 3 that she acted fraudulently, when read in context, Plaintiffs' allegations against
 4 Nancy Sitrick do appear to arise from a course of fraudulent conduct. The FAC
 5 unequivocally alleges that Nancy Sitrick made false or misleading statements of
 6 material fact, which resulted in damage to the value of the ESOP. (FAC ¶¶ 71(a),
 7 72–73.) The question then is whether Plaintiffs allege that she acted
 8 intentionally. It appears that they do. The FAC alleges that Nancy Sitrick was a
 9 conflicted fiduciary, who, from the face of the FAC, appears to have acted in
 10 furtherance of her husband's plan for their own financial gain. (*See id.* at ¶¶ 48,
 11 67.) As such, the FAC fails to plead with particularity the allegations in Count I
 12 against Nancy Sitrick. Accordingly, the Court finds that Count I, as against
 13 Nancy Sitrick, too fails to meet the heightened pleading standards required under
 14 Rule 9(b).³

15 For these reasons, the Court GRANTS the Sitricks' Motion as to Count I
 16 and dismisses *without prejudice* Count I as against Sitrick and Nancy Sitrick.

17 **2. Count II**

18 Plaintiffs assert Count II—for violation of Sections 406 and 408 of the
 19 ERISA, 29 U.S.C. §§ 1106 and 1108—against Sitrick, Nancy Sitrick, the Sitrick
 20 Trust, and Reliance. Section 406(a) prohibits ERISA fiduciaries from causing a
 21 plan to engage in transactions between the plan and a party in interest. 29 U.S.C.
 22 § 1106(a). Section 406(b) mandates that a fiduciary, himself, not engage in
 23 transactions with the plan. *Id.* at § 1106(b). Section 408 outlines various
 24 exemptions that do not give rise to liability. *Id.* at § 1108.

25
 26 ³ As stated, the Court dismisses Count I against Sitrick and Nancy Sitrick
 27 *without prejudice*. To the extent Plaintiffs do not contend that Nancy Sitrick's
 28 breaches of fiduciary duty arose from a fraudulent course of conduct, any amendment
 to the FAC must clearly indicate as much.

1 Plaintiffs allege that the Goodwill Purchase Transaction and 2008 Stock
2 Repurchase Transaction were prohibited transactions between a plan and parties
3 in interest. (FAC ¶ 76.) They claim that Sitrick and his wife were ERISA
4 fiduciaries who engaged in the Personal Goodwill Transaction (*id.* at ¶ 77) and
5 that Sitrick, his wife, and Reliance were ERISA fiduciaries who engaged in the
6 2008 Stock Repurchase Transaction (*id.* at ¶ 78).

7 *a. Section 406(a) — Personal Goodwill Transaction*

8 The Court first addresses whether Plaintiffs state a claim under Section
9 406(a) with respect to the Personal Goodwill Transaction. The Sitrick
10 Defendants argue that the Transaction is not actionable, because it was not caused
11 by a plan fiduciary. (Sitricks' Mem. 19.) They contend that because Sitrick was
12 acting in his "individual" and "corporate" capacities when he purportedly caused
13 the Transaction to occur, the FAC forecloses the interpretation that he was acting
14 as a plan fiduciary at the time. (*Id.* at 20.) The Court disagrees.

15 The Ninth Circuit has explained that where "an ESOP fiduciary also serves
16 as a corporate director or officer, imposing ERISA duties on business decisions
17 from which that individual could directly profit does not to us seem an
18 unworkable rule." *Johnson*, 572 F.3d at 1077. As such, because the Transaction
19 was a business decision that resulted in substantial pecuniary gain for Sitrick (and
20 his wife who allegedly profited from the financial success of the marital
21 community), the FAC adequately alleges that Sitrick and his wife were ERISA
22 fiduciaries when they purportedly caused the Transaction to occur.

23 In the alternative, the Sitrick Defendants contend that the Transaction did
24 not involve ESOP assets. (Sitricks' Mem. 20.) Because Sitrick purportedly
25 misappropriated and transferred to himself "corporate assets" (FAC ¶ 34), as
26 opposed to plan or ESOP assets, the Sitrick Defendants argue that the Transaction
27 was not prohibited. Based on the allegations in the FAC, the Court concurs.

28 Generally, corporate assets are not plan assets. *Johnson*, 572 F.3d at 1080.

1 Yet, as Plaintiffs argue, the Ninth Circuit has found that, in some instances, the
 2 use of corporate assets may be considered a diminution of plan assets. *Id.* In
 3 *Johnson v. Couturier*, a company's liquidation plan provided for payment of all
 4 remaining equity to ESOP participants. *Id.* As such, any funds used to
 5 compensate defendants or pay their legal expenses would, "dollar for dollar,
 6 reduce the funds available for distribution to ESOP participants." *Id.* "In other
 7 words," expenditure of company funds was "tantamount to asking ESOP
 8 participants to pay for Defendants' defense costs, with no recovery possible or at
 9 least highly unlikely..." *Id.*

10 Here, the FAC alleges that the Personal Goodwill Transaction involved an
 11 expenditure of "corporate assets." (FAC ¶ 34.) There is no allegation that the
 12 Transaction involved plan assets, such as shares owned by the ESOP. Although
 13 the Court recognizes that Sitrick and the ESOP were the only shareholders in SCI
 14 (*id.* at ¶ 22), the FAC contains no factual allegations suggesting that
 15 circumstances similar to those in *Johnson v. Couturier* are present. The FAC
 16 does not allege, for instance, that all remaining SCI equity would be paid to
 17 ESOP participants, such that a reduction in the company's equity would result in
 18 a direct loss to the ESOP. Nothing suggests how or in what manner the Personal
 19 Goodwill Transaction resulted in a "dollar for dollar" loss to the ESOP or was
 20 "tantamount" to asking ESOP participants to pay Sitricks' allegedly excessive
 21 compensation. *Johnson*, 572 F.3d at 1080. Simply put, the FAC is devoid of
 22 factual allegations allowing this Court to plausibly infer that ESOP assets were
 23 compromised through this Transaction.

24 Consequently, the Court finds that the FAC fails to state a claim for
 25 violation of Section 406(a) as it relates to the Personal Goodwill Transaction.

26 *b. Section 406(a) — 2008 Stock Repurchase Transaction*

27 Having found that the FAC fails to state a claim under Section 406(a) with
 28 respect to the Personal Goodwill Transaction, the Court now must consider

1 whether the FAC states a claim under Section 406(a) with regard to the Stock
2 Repurchase.

3 The Sitrick Defendants first argue that the FAC does not plausibly state a
4 claim under 406(a) with respect to the Stock Repurchase, because there is no
5 factual basis to conclude that they were acting as ERISA fiduciaries given that
6 SCI had hired Reliance to act as a plan fiduciary. (Sitricks' Mem. 21.) For the
7 reasons previously articulated, this argument is unavailing.

8 The Sitrick Defendants further contend that the FAC lacks a factual basis
9 suggesting that they are liable as parties in interest. (Sitricks' Mem. 22.) To be
10 liable as a party in interest under Section 406(a), an individual must "have had
11 actual or constructive knowledge of the circumstances that rendered the
12 transaction unlawful." *Harris Trust & Sav. Bank v. Salomon Smith Barney*, 530
13 U.S. 238, 251 (2000). Where a transaction provides "adequate consideration" for
14 a plan's shares, that transaction is not unlawful. 29 U.S.C. § 1108(a). The Sitrick
15 Defendants argue that the FAC lacks non-conclusory facts suggesting that the
16 ESOP did not receive adequate consideration for its shares or that the price for
17 those shares was not determined in good faith. (Sitricks' Mem. 22.) That
18 argument lacks merit.

19 As alleged, at the time of the Stock Repurchase, the ESOP owned nearly
20 25% of SCI's total equity. (FAC ¶ 22.) However, just as an offer to purchase
21 SCI for a sum in excess of \$70 million materialized, Sitrick and SCI, of which
22 Nancy Sitrick was a officer and director, hired Reliance to "consider and approve
23 the sale of all of the ESOP's Class B shares in SCI to the Sitrick Trust..." (*Id.* at
24 ¶¶ 44–45.) Although the ESOP shares had originally been valued at \$9.00 per
25 share, the company experienced prosperity since it established the ESOP, and
26 SCI had been valued at a sum in excess of \$70 million just prior to the Stock
27 Repurchase, the ESOP received only \$1.04 per share or \$1.7 million for its nearly
28 one-quarter interest in SCI. (*Id.* at ¶ 22, 27–29, 44.) Then, with the Sitrick Trust

1 owning 100% of all the equity in SCI, the company merged with Brincko
2 Associates, Inc. to form Sitrick Brincko Group, LLC as part of an arrangement
3 for Resources to acquire SCI's assets. (*Id.* at ¶ 59.) As part of Resources'
4 acquisition of Sitrick Brincko Group, LLC, Sitrick and the Sitrick Trust received
5 a sum in excess of \$92 million. (*Id.* at ¶ 62.) Based on these allegations, it is
6 plausible to conclude that the ESOP, when it received \$1.7 million, failed to
7 obtain adequate consideration for its one-quarter interest in a company valued in
8 excess of \$70 million. It is also reasonable to conclude that, as alleged, the
9 Sitrick Defendants failed to act in good faith and instead acted to capitalize on a
10 lucrative offer that eventually allowed them to pocket nearly \$100 million by
11 owning 100% of SCI's equity. For these reasons, Plaintiffs allege a sufficient
12 factual basis to conclude that Sitrick and his wife were parties in interest. As
13 such, Plaintiffs state a claim under Section 406(a) with respect to the Stock
14 Repurchase.

15 *b. Section 406(b)*

16 Finally, Defendants argue that the FAC fails, as a matter of law, to state a
17 claim under Section 406(b)(1). (Sitricks' Mem. 24.) Section 406(b)(1) prohibits
18 a plan fiduciary from dealing with the plan's assets in his or her own interest. 29
19 U.S.C. § 1106(b)(1). With respect to the Personal Goodwill Transaction,
20 Plaintiffs fail to state a claim, because, as previously stated, they have not
21 adequately alleged that the Transaction involved *plan* assets.

22 However, with respect to the Stock Repurchase, Plaintiffs do state a claim
23 under Section 406(b). As discussed, Plaintiffs have adequately alleged that
24 Sitrick and his wife were plan fiduciaries for purposes of the Stock Repurchase.
25 Contrary to the Sitrick Defendants' argument, Plaintiffs have adequately alleged
26 that the ESOP did not receive adequate consideration and thus that the Stock
27 Repurchase was not exempted under Section 408(e). For these reasons, although
28 Plaintiffs fail to state a claim under Section 406(b) with respect to the Personal

1 Goodwill Transaction, they do state a claim with regard to the Stock Repurchase.

2 Overall, the Court GRANTS IN PART and DENIES IN PART the
3 Sitricks' Motion as to Count II. The Court GRANTS the Motion and dismisses
4 Count II as it relates to the Personal Goodwill Transaction. The Court DENIES
5 the Motion and declines to dismiss Count II as it pertains to the Stock Repurchase
6 Transaction.

7 **3. Count III**

8 Plaintiffs assert Count III—for violation of Section 405 of the ERISA, 29
9 U.S.C. § 1105, against Sitrick, Nancy Sitrick, and Reliance. Under Section 405,
10 “a fiduciary with respect to a plan shall be liable for a breach of fiduciary
11 responsibility of another fiduciary with respect to the same plan...if he
12 participates knowingly in, or knowingly undertakes to conceal, an act or omission
13 of such other fiduciary, knowing such act or omission is a breach.” 29 U.S.C. §
14 1105(a)(1).

15 With respect to the Sitrick Defendants, the FAC alleges that they are liable
16 as “co-fiduciaries for each other’s breaches regarding the Personal Goodwill
17 Transaction and the Stock Repurchase Transaction, as each participated
18 knowingly in the other’s fiduciary breaches, each knowingly undertook to
19 conceal the other’s fiduciary breaches, and each failed to make a reasonable
20 effort to remedy the other’s fiduciary breaches.” (FAC ¶ 86.)

21 Although the Court disagrees with the Sitrick Defendants’ first argument
22 that they cannot be liable because they were not plan fiduciaries, the Court does
23 agree that the FAC fails to allege a sufficient factual basis to support the scienter
24 requirement in Section 405. (Sitricks’ Mem. 24.) While the FAC does set forth a
25 factual basis as to breaches of duty by both Sitrick and his wife, it fails to provide
26 facts from which the Court could infer “actual knowledge” of the other party’s
27 breaches. In their Opposition, Plaintiffs cite to Paragraphs 86 and 88 to suggest
28 that they did, in fact, provide an adequate factual basis. (Opp’n to Sitricks’ Mot.

50.) However, Paragraphs 86 and 88 contain conclusory legal allegations devoid of any factual underpinning. (FAC ¶¶ 86, 88.) Absent a factual basis to support Plaintiffs' claims of "actual knowledge" of a co-fiduciary's breaches, Plaintiffs fail to state a claim.

Accordingly, the Court GRANTS the Sitricks' Motion as to Count III and dismisses *without prejudice* Count III as against Sitrick and Nancy Sitrick.

4. Count IV

Lastly, Plaintiffs assert Count IV—for equitable remedies under Sections 409(a) and 501(a)(3) of the ERISA, 29 U.S.C. §§ 1109(a) and 1132(a)(3)—against the Sitrick Trust. The Sitrick Defendants' only argument is that, because all other claims should be dismissed, Count IV too must be dismissed, since it is derivative of Counts I through III. (Sitricks' Mem. 25.) Without addressing whether Count IV states an independent basis for relief, the Court DENIES the Sitricks' Motion as to Count IV, since Count II survives the Sitricks' Motion.

B. Reliance's Motion to Dismiss

Reliance seeks dismissal of all claims against Reliance under Federal Rule of Civil Procedure 12(b)(6). (Reliance's Mot. 1.) For the reasons herein, the Court dismisses Count III *without prejudice* and declines to dismiss the remaining claims as alleged against Reliance.

1. Count I

As stated, Plaintiffs assert Count I—for violation of Section 404 of the ERISA, 29 U.S.C. § 1104—against Sitrick, Nancy Sitrick, and Reliance. With respect to their claim against Reliance, Plaintiffs allege that the company "acted imprudently and breached its fiduciary duties to the ESOP" in many respects, particularly by failing to investigate or question the validity of the Personal Goodwill Transaction. (FAC ¶ 70.) Reliance seeks dismissal of Count I on the ground that various allegations in the FAC "simply did not occur."

1 (Reliance's Mem. 9.) They claim that a valuation report, of which this Court has
2 declined to take judicial notice, evidences that Reliance acted prudently and
3 loyally in the way it evaluated SCI's income. (*Id.*)

4 However, on a motion to dismiss, the Court may not render credibility
5 determinations as to the weight of evidence. Rather, the Court must accept as
6 true all factual allegations in the FAC and construe them in the light most
7 favorable to Plaintiffs. *Nursing Home*, 380 F.3d at 1229. To accept as true
8 Reliance's interpretation of this valuation report would flatly contradict this
9 established rule of law. In addition, the Court may not consider evidence outside
10 the Complaint, particularly that of which the Court has refused to take judicial
11 notice. *See McCalip*, 2008 U.S. Dist. LEXIS 87870, at *4; *see Jacobson*, 50 F.3d
12 at 1496. Since Plaintiffs dispute the valuation report's authenticity and as a result
13 the Court has declined to take judicial notice, the Court may not consider this
14 report in determining whether the FAC states a claim for relief. Accordingly, the
15 Court DENIES Reliance's Motion as to Count I.

16 **2. Count II**

17 Plaintiffs assert Count II—for violation of Sections 406 and 408 of the
18 ERISA, 29 U.S.C. §§ 1106 and 1108—against Sitrick, Nancy Sitrick, the Sitrick
19 Trust, and Reliance. Reliance argues that Plaintiffs fail to state a claim.
20 (Reliance's Mem. 10.) It argues that because Plaintiffs received adequate
21 consideration for their shares, the Stock Repurchase was not a prohibited
22 transaction pursuant to Section 408. (*Id.* at 10–11.) However, for the reasons
23 previously stated, the FAC sets forth an adequate factual basis to conclude that
24 the ESOP did *not* receive adequate consideration for its shares. Therefore, the
25 Court DENIES Reliance's Motion as to Count II.

26 **3. Count III**

27 Finally, Plaintiffs assert Count III—for violation of Section 405 of the
28 ERISA, 29 U.S.C. § 1105, against Sitrick, Nancy Sitrick, and Reliance. Plaintiffs

1 argue that Reliance turned a “blind eye” to the flaws in the Personal Goodwill
2 Transaction and thus participated “knowingly” in breaches of fiduciary duty by
3 Sitrick and his wife. (FAC ¶ 87.)

4 However, just as the FAC fails to allege a factual basis to support the
5 scienter requirement of a Section 405 claim against the Sitrick Defendants, the
6 FAC too fails to provide any facts from which the Court could reasonably
7 conclude that Reliance “knowingly” participated in or advanced the misconduct
8 of other fiduciaries. Turning a “blind eye” to the conduct of Sitrick and his wife
9 hardly supports an allegation that Reliance, with actual knowledge, concealed the
10 fiduciary breaches of others. Absent a factual basis to support Plaintiffs’ legal
11 conclusion that Reliance acted “knowingly,” the FAC fails to state a claim here.

12 Accordingly, the Court GRANTS Reliance’s Motion and dismisses Count
13 III *without prejudice* as it pertains to Reliance.

14 VI.

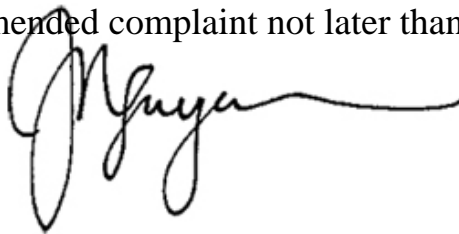
15 CONCLUSION

16 For these reasons, the Court GRANTS IN PART and DENIES IN PART
17 the Sitricks’ Motion (Docket No. 29). The Court GRANTS the Sitricks’ Motion
18 and dismisses *without prejudice* Count I, Count II (with respect to the Personal
19 Goodwill Transaction only) and Count III as alleged against Sitrick and Nancy
20 Sitrick. The Court DENIES the Sitricks’ Motion as to all remaining claims.

21 Additionally, the Court GRANTS IN PART and DENIES IN PART
22 Reliance’s Motion (Docket No. 30). The Court GRANTS Reliance’s Motion and
23 dismisses *without prejudice* Count III as alleged against Reliance. The Court
24 DENIES Reliance’s Motion as to all remaining claims.

25 Plaintiffs may file an amended complaint not later than September 10,
26 2010.

27 IT IS SO ORDERED.
28



1 Dated: August 10, 2010

2 Honorable Jacqueline H. Nguyen
3 UNITED STATES DISTRICT COURT
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